

**REPORT OF THE AUDIT OF THE
BREATHITT COUNTY
FISCAL COURT**

**For The Fiscal Year Ended
June 30, 2003**



**CRIT LUALLEN
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EXECUTIVE SUMMARY

AUDIT EXAMINATION OF THE BREATHITT COUNTY FISCAL COURT

**For The Fiscal Year Ended
June 30, 2003**

The Auditor of Public Accounts has completed the Breathitt County Fiscal Court audit for fiscal year ended June 30, 2003. We have issued an unqualified opinion on the financial statements taken as a whole. Based upon the audit work performed, the financial statements are presented fairly in all material respects.

Financial Condition:

Cash balances increased by \$7,492,008 from the beginning of the year, resulting in a cash surplus of \$8,926,468 as of June 30, 2003.

Debt Obligations:

Total debt principal as of June 30, 2003, was \$10,163,146. Future collections of \$13,903,979 are needed over the next twenty-one years to pay all bonded debt principal and interest.

Report Comments:

Compliance

- All Federal Awards Should Be Included In The County's Budget
- All Transactions Involving Federal Awards Should Be Properly Recorded On the 4th Quarter Financial Statement
- The County Should Require Depository Institutions To Enter Into A Written Collateral Security Agreement

Internal Control

- The Treasurer Should Post The Original Budget Amounts To The 4th Quarter Financial Statement

Internal Control – Single Audit

- The County Should Improve Subrecipient Monitoring Policies And Procedures
- The County Should Maintain Adequate Records Regarding Federal Awards

Deposits:

The fiscal court's deposits were insured and collateralized by bank securities or bonds.

Subsequent Events:

A. New Bond Issue

On July 10, 2003, the county issued \$865,000 in General Obligation Refunding Bonds to retire the Breathitt County Public Properties Corporation Series 1994 bonds and Series 1996 bonds, and a 1998 capital lease for a grader.

B. Hazardous Duty Retirement

On September 1, 2003, the county elected to allow the Breathitt County Sheriff's Department to begin participating in the hazardous duty retirement system. The county will pay the contribution rate for hazardous employees.

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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky

Honorable Ernie Fletcher, Governor

Robbie Rudolph, Secretary

Finance and Administration Cabinet

Honorable Lewis Warrix, Breathitt County Judge/Executive

Members of the Breathitt County Fiscal Court

Independent Auditor's Report

We have audited the accompanying statement of assets, liabilities, and equity arising from cash transactions of Breathitt County, Kentucky, as of June 30, 2003, and the related statement of cash receipts, cash disbursements, and changes in cash balances for the year then ended. These financial statements are the responsibility of the Breathitt County Fiscal Court. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, and the Audit Guide for Fiscal Court Audits issued by the Auditor of Public Accounts, Commonwealth of Kentucky. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, Breathitt County, Kentucky, prepares its financial statements on a prescribed basis of accounting that demonstrates compliance with the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets, liabilities, and fund balances of Breathitt County, Kentucky, as of June 30, 2003, and the revenues received and expenditures paid for the year then ended, in conformity with the modified cash basis of accounting.

In accordance with Government Auditing Standards, we have also issued our report dated March 23, 2004, on our consideration of Breathitt County, Kentucky's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.



To the People of Kentucky

Honorable Ernie Fletcher, Governor

Robbie Rudolph, Secretary

Finance and Administration Cabinet

Honorable Lewis Warrix, Breathitt County Judge/Executive

Members of the Breathitt County Fiscal Court

The accompanying financial information listed as supporting schedules in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements of Breathitt County, Kentucky. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Based on the results of our audit, we present the schedule of findings and questioned costs, included herein, which discusses the following report comments:

- All Federal Awards Should Be Included In The County's Budget
- All Transactions Involving Federal Awards Should Be Properly Recorded On The 4th Quarter Financial Statement
- The County Should Require Depository Institutions To Enter Into A Written Collateral Security Agreement
- The Treasurer Should Post The Original Budget Amounts To The 4th Quarter Financial Statement
- The County Should Improve Subrecipient Monitoring Policies And Procedures
- The County Should Maintain Adequate Records Regarding Federal Awards

Respectfully submitted,



Crit Luallen

Auditor of Public Accounts

Audit fieldwork completed -
March 23, 2004

BREATHITT COUNTY OFFICIALS

For The Fiscal Year Ended June 30, 2003

Fiscal Court Members:

Lewis Warrix	County Judge/Executive
James W. Combs	Commissioner
Steve Banks	Commissioner
Arch Turner	Commissioner

Other Elected Officials:

Brendon D. Miller	County Attorney
James E. Turner	Jailer
Tony Watts	County Clerk
Thomas E. Howard	Circuit Court Clerk
John L. Turner	Sheriff
Ervine Allen	Property Valuation Administrator
Bobby G. Thorpe, Jr.	Coroner

Appointed Personnel:

William K. Back	County Treasurer
Wanda Kay Barnett	Occupational Tax Collector
Brenda Fugate	Finance Officer

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STATEMENT OF ASSETS, LIABILITIES,
AND EQUITY ARISING FROM CASH TRANSACTIONS

BREATHITT COUNTY
STATEMENT OF ASSETS, LIABILITIES,
AND EQUITY ARISING FROM CASH TRANSACTIONS

June 30, 2003

	Governmental Fund Type			
	General	Special Revenue	Capital Projects	Debt Service
<u>Assets and Other Resources</u>				
<u>Assets</u>				
Cash and Cash Equivalents	\$ 694,693	\$ 188,916		
Restricted Cash-				
Capital Project Construction			7,746,159	
Public Properties Corporation				297,090
Total Assets	<u>\$ 694,693</u>	<u>\$ 188,916</u>	<u>\$ 7,746,159</u>	<u>\$ 297,090</u>
<u>Other Resources</u>				
Amounts to be provided				
in Future Years for:				
Loan Guaranty Payment	\$ 70,195	\$	\$	\$
Capital Lease	17,951			
Bond Payments				9,777,910
Total Other Resources	<u>\$ 88,146</u>	<u>\$</u>	<u>\$</u>	<u>\$ 9,777,910</u>
Total Assets and Other Resources	<u><u>\$ 782,839</u></u>	<u><u>\$ 188,916</u></u>	<u><u>\$ 7,746,159</u></u>	<u><u>\$ 10,075,000</u></u>

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
STATEMENT OF ASSETS, LIABILITIES, AND EQUITY
ARISING FROM CASH TRANSACTIONS
June 30, 2003
(Continued)

Totals
(Memorandum Only)

\$	70,195
	17,951
	555,000
	410,000
	8,030,000
	<u>1,080,000</u>
\$	<u>10,163,146</u>

\$	7,935,075
	<u>689,598</u>
\$	<u>8,624,673</u>
\$	<u><u>18,787,819</u></u>

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
 STATEMENT OF ASSETS, LIABILITIES, AND EQUITY
 ARISING FROM CASH TRANSACTIONS
 June 30, 2003
 (Continued)

	Governmental Fund Type			
	General	Special Revenue	Capital Projects	Debt Service
<u>Liabilities and Equity</u>				
<u>Liabilities</u>				
Loan Guaranty Payment (Note 6)	\$ 70,195	\$	\$	\$
Capital Leases (Note 5)	17,951			
Bonds:				
1994 Road Bond (Note 4A)				555,000
1996 Jail Bond (Note 4B)				410,000
2003 Kentucky Justice Center Bond (Note 4C)				8,030,000
2003 Bond Anticipation Note (Note 4D)				1,080,000
Total Liabilities	<u>\$ 88,146</u>	<u>\$</u>	<u>\$</u>	<u>\$ 10,075,000</u>
<u>Equity</u>				
Fund Balances:				
Reserved	\$	\$ 188,916	\$ 7,746,159	
Unreserved	<u>689,598</u>			
Total Equity	<u>\$ 689,598</u>	<u>\$ 188,916</u>	<u>\$ 7,746,159</u>	<u>\$</u>
Total Liabilities and Equity	<u><u>\$ 777,744</u></u>	<u><u>\$ 188,916</u></u>	<u><u>\$ 7,746,159</u></u>	<u><u>\$ 10,075,000</u></u>

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
STATEMENT OF ASSETS, LIABILITIES, AND EQUITY
ARISING FROM CASH TRANSACTIONS
June 30, 2003
(Continued)

Totals <u>(Memorandum Only)</u>	
\$	70,195
	17,951
	555,000
	410,000
	8,030,000
	<u>1,080,000</u>
\$	<u>10,163,146</u>
\$	7,935,075
	<u>689,598</u>
\$	<u>8,624,673</u>
\$	<u><u>18,787,819</u></u>

The accompanying notes are an integral part of the financial statements.

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STATEMENT OF CASH RECEIPTS,
CASH DISBURSEMENTS, AND CHANGES IN CASH BALANCES

BREATHITT COUNTY
STATEMENT OF CASH RECEIPTS,
CASH DISBURSEMENTS, AND CHANGES IN CASH BALANCES

For The Fiscal Year Ended June 30, 2003

	General Fund Type			
	General Fund	Road and Bridge Fund	Jail Fund	Local Government Economic Assistance Fund
<u>Cash Receipts</u>				
Schedule of Operating Revenue	\$ 1,612,088	\$ 1,284,968	\$ 81,261	\$ 271,650
Other Financing Sources:				
Grant Proceeds-Unbudgeted				
Receipts-Jail Incentive Account				
Transfers In	100,657	100,000	437,381	
Bond Proceeds				
Total Cash Receipts	<u>\$ 1,712,745</u>	<u>\$ 1,384,968</u>	<u>\$ 518,642</u>	<u>\$ 271,650</u>
<u>Cash Disbursements</u>				
Comparative Schedule of Final Budget and Budgeted Expenditures	\$ 1,276,982	\$ 908,157	\$ 479,590	\$ 246,083
Other Financing Uses:				
Schedule of Unbudgeted Expenditures				
Schedule of Capital Project Expenditures				
Schedule of Debt Service Expenditures				
Transfers Out	328,381	316,000	31,538	209,000
Bonds:				
Principal Paid				
Interest Paid				
Bond Anticipation Notes				
Principal Paid				
Interest Paid				
Loan Guaranty - Principal Paid				2,435
Capital Lease - Principal Paid	8,036	26,298	4,972	
Total Cash Disbursements	<u>\$ 1,613,399</u>	<u>\$ 1,250,455</u>	<u>\$ 516,100</u>	<u>\$ 457,518</u>
Excess (Deficiency) of Cash Receipts Over (Under) Cash Disbursements	\$ 99,346	\$ 134,513	\$ 2,542	\$ (185,868)
Cash Balance - July 1, 2002	<u>\$ 312,976</u>	<u>\$ 22,343</u>	<u>\$ 16,452</u>	<u>\$ 291,999</u>
			*	
Cash Balance - June 30, 2003	<u>\$ 412,322</u>	<u>\$ 156,856</u>	<u>\$ 18,994</u>	<u>\$ 106,131</u>

* Increase Prior Year Carry Over Cash Balance \$1.00 for report presentation.

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
 STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND
 CHANGES IN CASH BALANCES
 For The Fiscal Year Ended June 30, 2003
 (Continued)

Special Revenue Fund Type				
Jail Incentive Pay Fund	Solid Waste Fund	E-911 Fund	Local Government Economic Development Fund	Industrial Foundation Pass Through Grant Fund
	\$ 213,405	\$ 92,122	\$ 300,000	
3,632				753,817
<u>\$ 3,632</u>	<u>\$ 213,405</u>	<u>\$ 92,122</u>	<u>\$ 300,000</u>	<u>\$ 753,817</u>
\$	\$ 130,477	\$ 77,735	\$ 347,603	
				753,817
<u>\$</u>	<u>\$ 130,477</u>	<u>\$ 77,735</u>	<u>\$ 347,603</u>	<u>\$ 753,817</u>
\$ 3,632	\$ 82,928	\$ 14,387	\$ (47,603)	\$
\$ 1,480	\$ 31,935	\$ 51,549	\$ 50,608	\$
		*	*	
<u>\$ 5,112</u>	<u>\$ 114,863</u>	<u>\$ 65,936</u>	<u>\$ 3,005</u>	<u>\$</u>

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
 STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND
 CHANGES IN CASH BALANCES
 For The Fiscal Year Ended June 30, 2003
 (Continued)

	Capital Projects Fund Type	
		Breathitt County Kentucky Justice Center Corporation Construction Fund
<u>Cash Receipts</u>	<u>Capital Projects Fund</u>	<u>Fund</u>
Schedule of Operating Revenue		\$ 3,789
Other Financing Sources:		
Grant Proceeds-Unbudgeted		
Receipts-Jail Incentive Account		
Transfers In		6,717,950
Bond Proceeds		9,998,117
Total Cash Receipts	<u>\$</u>	<u>\$ 16,719,856</u>
<u>Cash Disbursements</u>		
Comparative Schedule of Final Budget and Budgeted Expenditures		\$
Other Financing Uses:		
Schedule of Unbudgeted Expenditures		
Schedule of Capital Project Expenditures		557,700
Schedule of Debt Service Expenditures		
Transfers Out	657	8,783,906
Bonds:		
Principal Paid		
Interest Paid		
Bond Anticipation Notes		
Principal Paid		
Interest Paid		
Loan Guaranty - Principal Paid		
Capital Lease - Principal Paid		
Total Cash Disbursements	<u>\$ 657</u>	<u>\$ 9,341,606</u>
Excess (Deficiency) of Cash Receipts Over (Under) Cash Disbursements	\$ (657)	\$ 7,378,250
Cash Balance - July 1, 2002	<u>\$ 657</u>	<u>\$ 367,909</u>
Cash Balance - June 30, 2003	<u>\$</u>	<u>\$ 7,746,159</u>

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
 STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND
 CHANGES IN CASH BALANCES
 For The Fiscal Year Ended June 30, 2003
 (Continued)

Debt Service Fund Type		
Breathitt County Kentucky Justice Center Corporation Bond Fund	Breathitt County Public Properties Corporation Bond Fund	Totals (Memorandum Only)
\$	\$ 7,085	\$ 3,866,368
		753,817
		3,632
2,065,956	247,538	9,669,482
		9,998,117
<u>\$ 2,065,956</u>	<u>\$ 254,623</u>	<u>\$ 24,291,416</u>
\$	\$	\$ 3,466,627
		753,817
		557,700
	2	2
		9,669,482
	170,000	170,000
	74,083	74,083
2,045,000		2,045,000
20,956		20,956
		2,435
		39,306
<u>\$ 2,065,956</u>	<u>\$ 244,085</u>	<u>\$ 16,799,408</u>
\$	\$ 10,538	\$ 7,492,008
	\$ 286,552	\$ 1,434,460
<u>\$</u>	<u>\$ 297,090</u>	<u>\$ 8,926,468</u>

The accompanying notes are an integral part of the financial statements.

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS

June 30, 2003

Note 1. Summary of Significant Accounting Policies

A. Reporting Entity

The financial statements of Breathitt County include the funds, agencies, boards, and entities for which the fiscal court is financially accountable. Financial accountability, as defined by Section 2100 of the GASB Codification of Governmental Accounting and Financial Reporting Standards, as amended by GASB 14, was determined on the basis of the government's ability to significantly influence operations, select the governing authority, participate in fiscal management and the scope of public service. Based upon the application of the criteria stated in GASB 14, management has included the Breathitt County Public Properties Corporation (PPC) and the Breathitt County Kentucky Justice Center Corporation (JCC) as part of the reporting entity.

Breathitt County Public Properties Corporation

The Fiscal Court has the authority to appoint a voting majority of the Breathitt County Public Properties Corporation's Board of Directors. The Fiscal Court also has the ability to approve or modify the PPC's budget, approve or modify rate or fee changes affecting revenues, veto, overrule, or modify decisions of Board of Directors, or otherwise impose its will on the PPC. In addition, the Fiscal Court is financially accountable for the PPC, legally entitled to the PPC's resources, as well as legally obligated for the PPC's debt. Financial information for the Breathitt County Public Properties Corporation is blended within Breathitt County's financial statements.

Breathitt County Kentucky Justice Center Corporation

The Fiscal Court has the ability to approve or modify the JCC's budget, approve or modify rate or fee changes affecting revenues, veto, overrule, or modify decisions of Board of Directors, or otherwise impose its will on the JCC. In addition, the Fiscal Court is financially accountable for the PPC, legally entitled to the JCC's resources, as well as legally obligated for the JCC's debt. Financial information for the Breathitt County Kentucky Justice Center Corporation is blended within Breathitt County's financial statements.

Additional - Breathitt County Constitutional Elected Officials

- Circuit Court Clerk
- County Attorney
- County Clerk
- County Sheriff
- Property Valuation Administrator

The Kentucky constitution provides for election of the above officials from the geographic area constituting Breathitt County. Pursuant to state statute, these officials perform various services for the Commonwealth of Kentucky, its judicial courts, the fiscal court, various cities and special districts within the county, and the board of education. In exercising these responsibilities, however, they are required to comply with state laws. Audits of their financial statements are issued separately and individually and can be obtained from their respective administrative offices.

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

B. Fund Accounting

Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. The government uses funds to report on its financial position and the results of its operations. A fund is a separate accounting entity with a self-balancing set of accounts. Breathitt County Fiscal Court's Fund Types, a definition of each, and county funds included within each fund type are listed below.

1) General Fund Type

General Fund Type accounts for all financial resources except those required to be accounted for in another fund type. The Breathitt County General Fund Type includes the following county funds: General Fund, Road and Bridge Fund, Jail Fund, Local Government Economic Assistance Fund.

2) Special Revenue Fund Type

Special Revenue Fund Type accounts for the proceeds of specific revenue sources that are legally restricted to expenditures for the specified purpose. The Breathitt County Special Revenue Fund Type includes the following county funds: Jail Incentive Pay Fund, Solid Waste Fund, E-911 Fund, Local Government Economic Development Fund, and the Industrial Foundation Pass Through Grant Fund.

3) Capital Projects Fund Type

Capital Projects Fund Type accounts for financial resources to be used for acquisition of major capital facilities. The Capital Projects Fund and the Breathitt County Kentucky Justice Center Corporation Construction Fund of the Fiscal Court are reported as a Capital Projects Fund Type.

4) Debt Service Fund Type

Debt Service Fund Type accounts for the accumulation of resources for the payment of general long-term debt principal and interest and includes funds for the Breathitt County Public Properties Corporation Bond Fund and the Breathitt County Kentucky Justice Center Corporation Bond Fund. Debt service is provided through annual transfers from the General Fund Type in the amount of the debt service requirements for the year.

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting

For all fund types, the county utilizes a modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under this basis of accounting, assets, liabilities, and related revenues and expenditures are recorded when they result from cash transactions, with a few exceptions. This modified cash basis recognizes revenues when received and expenditures when paid. Long-term receivables deferred revenue, long-term obligations and amounts to be provided in future years to retire debt are recorded in the financial statements. The amount to be provided in future years to retire debt is offset by any cash or cash equivalents held by the county in a bond or debt service fund.

The State Local Finance Officer does not require the county to maintain a general fixed assets group of accounts; therefore the value to the county's fixed assets is not included in the financial statements. These fixed assets include buildings, equipment and land that are owned by the county.

D. Legal Compliance - Budget

The Breathitt County budget is adopted on a cash basis of accounting and according to the laws of Kentucky as required by the State Local Finance Officer. The County Judge/Executive is required to submit estimated receipts and proposed expenditures to the Fiscal Court by May 1 of each year. The budget is prepared by fund, function, and activity and is required to be adopted by the fiscal court by July 1.

The Fiscal Court may change the original budget by transferring appropriations at the activity level; however, the Fiscal Court may not increase the total budget without approval by the State Local Finance Officer. Expenditures may not exceed budgeted appropriations at the activity level.

Formal budgets are not adopted for the Breathitt County Public Properties Corporation Bond Fund (Debt Service Fund Type), the Breathitt County Kentucky Justice Center Corporation Bond Fund (Debt Service Fund Type), and the Breathitt County Kentucky Justice Center Corporation Construction Fund (Capital Projects Fund Type). The Department for Local Government does not require these funds to be budgeted.

E. Cash and Investments

Cash includes amounts in bank accounts, and investments are stated at cost. For the purpose of the statement of cash flows, the county considers all investments with a maturity date of three months or less when purchased to be cash equivalents.

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 1. Summary of Significant Accounting Policies (Continued)

E. Cash and Investments (Continued)

KRS 66.480 authorizes the county to invest in the following, including but not limited to, obligations of the United States and of its agencies and instrumentalities, obligations and contracts for future delivery or purchase of obligations backed by the full faith and credit of the United States, obligations of any corporation of the United States government, bonds or certificates of indebtedness of this state, and certificates of deposit issued by or other interest-bearing accounts of any bank or savings and loan institution which are insured by the Federal Deposit Insurance Corporation (FDIC) or which are collateralized, to the extent uninsured, by any obligation permitted by KRS 41.240(4).

F. Related Organizations

A related organization is an entity for which a primary government is not financially accountable. It does not impose will or have a financial benefit or burden relationship, even if the primary government appoints a voting majority of the related organization's governing board. Based on these criteria, the following is considered a related organization of Breathitt County Fiscal Court: Breathitt County Industrial Foundation.

G. Jointly Governed Organizations

A jointly governed organization is an entity that results from a multigovernmental arrangement that is governed by representatives from each participating government. The entity provides services to the citizens of each participating government, but there is no ongoing financial interest or responsibility by the participating governments. The jointly governed organization can act independently of each of the participating governments. The Jackson/Breathitt County Airport Board meets the criteria noted above and is disclosed as an organization jointly governed by the Breathitt County and the City of Jackson.

Note 2. Employee Retirement System

The county has elected to participate in the County Employees Retirement System (CERS), pursuant to KRS 78.530 administered by the Board of Trustees of the Kentucky Retirement Systems. This is a multiple-employer public retirement system which covers all eligible full-time employees. Benefit contributions and provisions are established by statute. Nonhazardous covered employees are required to contribute 5 percent of their salary to the plan. The county's contribution rate for nonhazardous employees was 6.34 percent.

Benefits fully vest on reaching five years of service for nonhazardous employees. Aspects of benefits for nonhazardous employees include retirement after 27 years of service or age 65.

Historical trend information showing the CERS' progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement Systems' annual financial report.

BREATHITT COUNTY
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2003
 (Continued)

Note 3. Deposits

The county maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the county and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. The depository institution has pledged or provided sufficient collateral, and the depository institution's board of directors or loan committee approved the pledge or provision. However, the depository institution did not have a written agreement with the county securing the county's interest in the collateral.

Note 4. Long-Term Debt

A. Breathitt County Public Properties Corporation - 1994 Road Bond

In March 1994, the Breathitt County Public Properties Corporation, a component unit of the Breathitt County Fiscal Court, issued \$1,745,000 in Public Project Revenue Bonds to retire a 1989 bond issue and to finance road projects within the County. These bonds are scheduled to mature in April 2006; interest payments are due every six months starting in October 1994 and principal payments are due annually beginning in April 1995. At June 30, 2003, the principal balance outstanding on these bonds was \$555,000. Debt service requirements for fiscal years ending June 30, 2004, and thereafter are as follows:

<u>Fiscal Year Ended</u> <u>June 30</u>	<u>Scheduled</u> <u>Interest</u>	<u>Scheduled</u> <u>Principal</u>
2004	\$ 35,900	\$ 175,000
2005	24,700	185,000
2006	<u>12,675</u>	<u>195,000</u>
Totals	<u>\$ 73,275</u>	<u>\$ 555,000</u>

BREATHITT COUNTY
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2003
 (Continued)

Note 4. Long-Term Debt (Continued)

B. Breathitt County Public Properties Corporation - 1996 Jail Bond

In February 1996, the Breathitt County Public Properties Corporation, a component unit of the Breathitt County Fiscal Court, issued \$445,000 in Public Project Revenue Bonds to the cost of renovating the existing county detention center. These bonds are scheduled to mature in February 2016; interest payments are due every six months starting in August 1996 and principal payments are due annually beginning in February 1997. At June 30, 2003, the principal balance outstanding on these bonds was \$410,000. Debt service requirements for fiscal years ending June 30, 2004, and thereafter are as follows:

Fiscal Year Ended June 30	Scheduled Interest	Scheduled Principal
2004	\$ 26,520	\$ 5,000
2005	26,215	15,000
2006	25,285	20,000
2007	24,025	25,000
2008	22,425	25,000
2009-2013	85,475	155,000
2014-2016	24,375	165,000
Totals	<u>\$ 234,320</u>	<u>\$ 410,000</u>

C. Breathitt County, Kentucky Justice Center Corporation Bond

On April 1, 2003, the Breathitt County, Kentucky Justice Center Corporation issued bonds in order to construct a new Justice Center. On the same day, the Breathitt County, Kentucky Justice Center Corporation, Administrative Office of the Courts (AOC), and the county entered into a lease agreement for the purpose of obtaining office rental space for the AOC at the Justice Center.

The Breathitt County, Kentucky Justice Center Corporation is acting as an agent for the AOC in order to plan, design, construct, manage and maintain the Justice Center. The Breathitt County, Kentucky Justice Center Corporation expects annual rentals for use of the Justice Center to be in the full amount of the annual principal and interest requirements of the bonds. Under the terms of the lease, the AOC has agreed to pay directly to the paying agent bank, the use allowance payment as provided in the lease. The lease agreement is renewable every two years. The Breathitt County, Kentucky Justice Center Corporation is in reliance upon the use allowance payment in order to meet the debt service for the bonds.

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 4. Long-Term Debt (Continued)

C. Breathitt County, Kentucky Justice Center Corporation Bond (Continued)

The use allowance payment commences with occupancy of the Judicial Building by the AOC. The AOC with the execution of the lease has expressed its intention to continue to pay the full use allowance payment in each successive biennial budget for a period of twenty years, but the lease does not legally obligate the AOC to do so. As of June 30, 2003, the principal balance outstanding was \$8,030,000. Debt service requirements for fiscal years ending June 30, 2004, and thereafter are as follows:

<u>Fiscal Year Ended</u> <u>June 30</u>	<u>Scheduled</u> <u>Interest</u>	<u>Scheduled</u> <u>Principal</u>
2004	\$ 287,780	\$
2005	283,430	290,000
2006	274,655	295,000
2007	265,655	305,000
2008	256,355	315,000
2009-2013	1,127,287	1,730,000
2014-2018	803,565	2,050,000
2019-2023	368,500	2,485,000
2024	11,200	560,000
Totals	<u>\$ 3,678,427</u>	<u>\$ 8,030,000</u>

D. Bond Anticipation Notes

First Mortgage Revenue Bond Anticipation Notes, Series 2001

On September 18, 2001, the Breathitt County, Kentucky Justice Center Corporation, a component entity of the Breathitt County Fiscal Court, issued \$1,000,000 of bond anticipation notes to finance the initial construction costs for a new Justice Center. The notes matured in August 1, 2002. The principal due of \$1,000,000 and interest due of \$13,600 were paid in full.

First Mortgage Revenue Bond Anticipation Renewal Notes, Series 2002

On July 31, 2002, the Breathitt County, Kentucky Justice Center Corporation, a component entity of the Breathitt County Fiscal Court, issued \$1,045,000 of bond anticipation renewal notes to finance the initial construction costs for a new Justice Center. The notes matured on February 1, 2003. The principal due of \$1,045,000 and interest due of \$7,356 were paid in full.

BREATHITT COUNTY
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2003
 (Continued)

Note 4. Long-Term Debt (Continued)

D. Bond Anticipation Notes (Continued)

First Mortgage Revenue Bond Anticipation Renewal Notes, Series 2003

On January 30, 2003, the Breathitt County, Kentucky Justice Center Corporation, a component unit of the Breathitt County Fiscal Court, issued \$1,080,000 of bond anticipation renewal notes to finance the initial construction costs for a new Justice Center. The notes mature on August 1, 2003. The principal of \$1,080,000 and interest of \$13,575 is due on August 1, 2003.

Note 5. Capital Leases

A. 1999 Chevy Tahoe

On January 8, 1999, the County entered into a lease agreement with Citizens Bank for the purchase of a 1999 Chevy Tahoe. Terms of the lease agreement stipulate a four-year repayment schedule with monthly principal and interest payments. The final lease payment on the Tahoe was made in FY 2003.

B. Grader

On December 9, 1998, the County entered into a lease agreement with Citizens Bank for the purchase of a grader. Terms of the lease agreement stipulate a five-year repayment schedule with monthly principal and interest payments of \$2,306. As of June 30, 2003, the principal balance outstanding was \$8,229. Future debt service requirements are as follows:

<u>Fiscal Year Ended</u> <u>June 30</u>	<u>Scheduled</u> <u>Interest</u>	<u>Scheduled</u> <u>Principal</u>
2004	\$ 236	\$ 8,229
Totals	<u>\$ 236</u>	<u>\$ 8,229</u>

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 5. Capital Leases (Continued)

C. 2002 Chevy Suburban

On April 23, 2002, the County entered into a lease agreement with Citizens Bank for the purchase of a 2002 Chevy Suburban. Terms of the lease agreement stipulate a three-year repayment schedule with monthly principal and interest payments of \$506. As of June 30, 2003, the principal balance outstanding was \$9,722. Debt service requirements for fiscal years ending June 30, 2004 and thereafter are as follows:

Fiscal Year Ended June 30	Scheduled Interest	Scheduled Principal
2004	\$ 403	\$ 5,668
2005	114	4,054
Totals	<u>\$ 517</u>	<u>\$ 9,722</u>

Note 6. Loan Guaranty

Airport Board

On November 1, 1999, the County and the City of Jackson entered into an unsecured guaranty agreement with First National Bank. The agreement stipulates that the County and the City of Jackson will guarantee payments on a loan that was entered into by the Jackson/Breathitt Airport Board in the amount of \$156,317. Terms of the agreement stipulate a principal and interest payment of \$1,000 per month with a termination date of November 16, 2019. The County and the City of Jackson currently pay an equal payment of \$500 each directly to First National Bank. As of June 30, 2003, the County's portion of the principal balance outstanding was \$70,195. Debt service requirements for the County's portion for fiscal years ending June 30, 2004 and thereafter are as follows:

Fiscal Year Ended June 30	Scheduled Interest	Scheduled Principal
2004	\$ 3,450	\$ 2,550
2005	3,310	2,690
2006	3,172	2,828
2007	3,028	2,972
2008	2,884	3,116
2009-2013	11,819	18,181
2014-2018	6,667	23,333
2019-2020	3,243	14,525
Totals	<u>\$ 37,573</u>	<u>\$ 70,195</u>

BREATHITT COUNTY
NOTES TO FINANCIAL STATEMENTS
June 30, 2003
(Continued)

Note 7. Subsequent Events

A. New Bond Issue

On July 10, 2003, the County issued \$865,000 in General Obligation Refunding Bonds to retire the Breathitt County Public Properties Corporation Series 1994 bonds and Series 1996 bonds, and a 1998 capital lease for a grader.

B. Hazardous Duty Retirement

On September 1, 2003, the County elected to allow the Breathitt County Sheriff's Department to begin participating in the hazardous duty retirement system. The contribution rate for hazardous employees will be paid by the County.

Note 8. Insurance

For the fiscal year ended June 30, 2003, Breathitt County was a member of the Kentucky Association of Counties' All Lines Fund (KALF). KALF is a self-insurance fund and was organized to obtain lower cost coverage for general liability, property damage, public officials' errors and omissions, public liability, and other damages. The basic nature of a self-insurance program is that of a collectively shared risk by its members. If losses incurred for covered claims exceed the resources contributed by the members, the members are responsible for payment of the excess losses.

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COMPARATIVE SCHEDULE OF
BUDGETED TO ACTUAL OPERATING REVENUE

BREATHITT COUNTY
COMPARATIVE SCHEDULE OF
BUDGETED TO ACTUAL OPERATING REVENUE

For The Fiscal Year Ended June 30, 2003

<u>Budgeted Funds</u>	<u>Budgeted Operating Revenue</u>	<u>Actual Operating Revenue</u>	<u>Over (Under) Budget</u>
<u>General Fund Type</u>			
General Fund	\$ 1,393,310	\$ 1,612,088	\$ 218,778
Road and Bridge Fund	1,719,454	1,284,968	(434,486)
Jail Fund	93,960	81,261	(12,699)
Local Government Economic Assistance Fund	347,228	271,650	(75,578)
<u>Special Revenue Fund Type</u>			
Solid Waste Fund	167,472	213,405	45,933
E-911 Fund	100,500	92,122	(8,378)
Local Government Economic Development Fund	<u>354,736</u>	<u>300,000</u>	<u>(54,736)</u>
Totals	<u>\$ 4,176,660</u>	<u>\$ 3,855,494</u>	<u>\$ (321,166)</u>
<u>Reconciliation</u>			
Total Budgeted Operating Revenue Above			\$ 4,176,660
Add: Budgeted Prior Year Surplus			814,278
Less: Other Financing Uses			<u>(289,279)</u>
Total Operating Budget Per Comparative Schedule Of Final Budget and Budgeted Expenditures			<u>\$ 4,701,659</u>

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SCHEDULE OF OPERATING REVENUE

BREATHITT COUNTY
SCHEDULE OF OPERATING REVENUE

For The Fiscal Year Ended June 30, 2003

Revenue Categories	Governmental Fund Type				Totals (Memorandum Only)
	General Fund Type	Special Revenue Fund Type	Capital Projects Fund Type	Debt Service Fund Type	
Taxes	\$ 1,212,364	\$ 91,668	\$	\$	\$ 1,304,032
Excess Fees	16,412				16,412
Intergovernmental Revenues	1,812,194	451,403			2,263,597
Charges for Services	370	60,241			60,611
Miscellaneous Revenues	202,391	1,442			203,833
Interest Earned	6,236	773	3,789	7,085	17,883
Total Operating Revenue	<u>\$ 3,249,967</u>	<u>\$ 605,527</u>	<u>\$ 3,789</u>	<u>\$ 7,085</u>	<u>\$ 3,866,368</u>

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COMPARATIVE SCHEDULE OF
FINAL BUDGET AND BUDGETED EXPENDITURES

BREATHITT COUNTY
COMPARATIVE SCHEDULE OF
FINAL BUDGET AND BUDGETED EXPENDITURES

For The Fiscal Year Ended June 30, 2003

Expenditure Categories	General Fund Type		
	Final Budget	Budgeted Expenditures	Under (Over) Budget
General Government	\$ 994,130	\$ 821,878	\$ 172,252
Protection to Persons and Property	603,703	554,150	49,553
General Health and Sanitation	143,565	128,550	15,015
Social Services	24,563	22,863	1,700
Recreation and Culture	8,618	6,978	1,640
Transportation, Facilities and Services	5,000	1,114	3,886
Roads	1,158,854	807,477	351,377
Airports	12,565	13,848	(1,283)
Debt Service	249,000	1	248,999
Capital Projects	5,618	5,617	1
Administration	789,852	548,336	241,516
Total Operating Budget - All General Fund Types	\$ 3,995,468	\$ 2,910,812	\$ 1,084,656
Other Financing Uses:			
Transfers to Breathitt County Public Properties Corporation Bond Fund-	247,538	247,538	
Other County Liabilities			
Airport Board Principal	2,435	2,435	
Capital Lease Payments:			
Chevy Tahoe	8,036	8,036	
Grader	26,298	26,298	
Chevy Suburban	4,972	4,972	
TOTAL BUDGET - ALL GENERAL FUND TYPES	<u>\$ 4,284,747</u>	<u>\$ 3,200,091</u>	<u>\$ 1,084,656</u>

BREATHITT COUNTY
 COMPARATIVE SCHEDULE OF
 FINAL BUDGET AND BUDGETED EXPENDITURES
 For The Fiscal Year Ended June 30, 2003
 (Continued)

Expenditure Categories	Special Revenue Fund Type		
	Final Budget	Budgeted Expenditures	Under (Over) Budget
Protection to Persons and Property	\$ 94,019	\$ 72,299	\$ 21,720
General Health and Sanitation	185,133	122,023	63,110
Recreation and Culture	45,900	45,900	
Capital Projects	308,836	301,703	7,133
Administration	72,303	13,890	58,413
TOTAL BUDGET - SPECIAL REVENUE FUND TYPE	\$ 706,191	\$ 555,815	\$ 150,376

SCHEDULE OF UNBUDGETED EXPENDITURES

BREATHITT COUNTY
SCHEDULE OF UNBUDGETED EXPENDITURES

For The Fiscal Year Ended June 30, 2003

<u>Expenditure Items</u>	<u>Industrial Foundation Pass-Through Grant Fund</u>
Pass-Through to the Breathitt County Industrial Foundation	<u>\$ 753,817</u>
Total	<u><u>\$ 753,817</u></u>

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SCHEDULE OF BREATHITT COUNTY, KENTUCKY
JUSTICE CENTER CORPORATION CONSTRUCTION FUND EXPENDITURES

BREATHITT COUNTY
SCHEDULE OF BREATHITT COUNTY, KENTUCKY
JUSTICE CENTER CORPORATION CONSTRUCTION FUND EXPENDITURES

For The Fiscal Year Ended June 30, 2003

<u>Expenditure Items</u>	<u>Kentucky Justice Center Corporation Construction Fund</u>
Construction Costs	\$ 420,057
Fees	<u>137,643</u>
Totals	<u><u>\$ 557,700</u></u>

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SCHEDULE OF DEBT SERVICE EXPENDITURES

BREATHITT COUNTY
SCHEDULE OF DEBT SERVICE EXPENDITURES

Fiscal Year Ended June 30, 2003

<u>Expenditure Items</u>	<u>Public Properties Corporation Bond Fund</u>
Fees	<u>\$ 2</u>
Totals	<u><u>\$ 2</u></u>

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REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER
FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

Honorable Lewis Warrix, Breathitt County Judge/Executive
Members of the Breathitt County Fiscal Court

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards

We have audited the financial statements of Breathitt County, Kentucky, as of and for the year ended June 30, 2003, and have issued our report thereon dated March 23, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether Breathitt County's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs.

- Reference Number 2003-1: The County Should Require Depository Institutions To Enter Into A Written Collateral Security Agreement
- Reference Number 2003-2: All Federal Awards Should Be Included In The County's Budget
- Reference Number 2003-3: All Transactions Involving Federal Awards Should Be Properly Recorded On The 4th Quarter Financial Statement

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Breathitt County's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition.

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of Financial
Statements Performed In Accordance With Government Auditing Standards
(Continued)

Internal Control Over Financial Reporting (Continued)

Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect Breathitt County's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. A reportable condition is described in the accompanying schedule of findings and questioned costs.

- Reference Number 2003-4: The Treasurer Should Post The Original Budget Amounts To The 4th Quarter Financial Statement

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable condition described above is a material weakness.

This report is intended solely for the information and use of management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than the specified parties.

Respectfully submitted,



Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
March 23, 2004

REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL
CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

Honorable Lewis Warrix, Breathitt County Judge/Executive
Members of the Breathitt County Fiscal Court

Report On Compliance With Requirements
Applicable To Each Major Program And On Internal Control
Over Compliance In Accordance With OMB Circular A-133

Compliance

We have audited the compliance of Breathitt County, Kentucky, with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2003. Breathitt County's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Breathitt County's management. Our responsibility is to express an opinion on Breathitt County's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Breathitt County's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Breathitt County's compliance with those requirements.

In our opinion, Breathitt County complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2003.

Internal Control Over Compliance

The management of Breathitt County is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Breathitt County's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Report On Compliance With Requirements
Applicable To Each Major Program And On Internal Control
Over Compliance In Accordance With OMB Circular A-133
(Continued)

Internal Control Over Compliance (Continued)

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect Breathitt County's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs.

- Reference Number 2003-5: The County Should Improve Subrecipient Monitoring Policies And Procedures
- Reference Number 2003-6: The County Should Maintain Adequate Records Regarding Federal Awards

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable conditions described above are not material weaknesses.

This report is intended solely for the information and use of management, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than the specified parties.

Respectfully submitted,



Crit Luallen
Auditor of Public Accounts

Audit fieldwork completed -
March 23, 2004

FINDINGS AND QUESTIONED COSTS

BREATHITT COUNTY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For The Fiscal Year Ended June 30, 2003

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of Breathitt County.
2. One reportable condition disclosed during the audit of the financial statements is reported in the Independent Auditor's Report. The condition is reported as a material weakness.
3. Three instances of noncompliance material to the financial statements of Breathitt County were disclosed during the audit.
4. Two reportable conditions disclosed during the audit of the major federal awards programs are reported in the Independent Auditor's Report. The conditions are not reported as material weaknesses.
5. The auditor's report on compliance for the audit of the major federal awards programs for Breathitt County expresses an unqualified opinion.
6. Audit findings relative to the major federal awards programs for Breathitt County are reported in Part C of this schedule.
7. The programs tested as major programs were: (Community Development Block Grant, CFDA # 14.228; Appalachian Regional Commission Grant, CFDA # 23.002; Rural Development Community Facilities Grant, CFDA # 10.766).
8. The threshold for distinguishing Type A and B programs was \$300,000.
9. Breathitt County was not determined to be a low-risk auditee.

B. FINDINGS – FINANCIAL STATEMENTS AUDIT

NONCOMPLIANCES

Reference Number 2003-1

The County Should Require Depository Institutions To Enter Into A Written Collateral Security Agreement

The county maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between the county and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institutions or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution's board of directors or loan committee approving the pledge or provision. However, the depository institution did not have a written agreement with the county securing the county's interest in the collateral.

County Judge/Executive Lewis Warrix' Response: Will contact bank to resolve issue.

Report On Compliance With Requirements
Applicable To Each Major Program And On Internal Control
Over Compliance In Accordance With OMB Circular A-133
(Continued)

NONCOMPLIANCES (Continued)

Reference Number 2003-2

All Federal Awards Should Be Included In The County's Budget

The County did not include pass through federal awards in their original budget/budget amendments. Federal awards, even on a pass through basis, should be included in the county's budget and should be accounted for in a separate fund, when required. We recommend that the fiscal court include all federal awards in their budget in the future.

County Judge/Executive Lewis Warrix' Response: Will set up fund for pass-thru money.

Reference Number 2003-3

All Transactions Involving Federal Awards Should Be Properly Recorded On The 4th Quarter Financial Statement

The County did not record transactions involving federal awards passed through to the Industrial Foundation in the financial records. Pass through grants should be accounted for in the same manner as all other county transactions, that is, in accordance with the uniform system of accounts as presented in the *State Local Finance Officer Policy Manual* issued by the Department for Local Government. We recommend that the county account for pass through grants in their financial statements.

County Judge/Executive Lewis Warrix' Response: Will set up fund for pass-thru money.

REPORTABLE CONDITIONS

Reference Number 2003-4

The Treasurer Should Post The Original Budget Amounts To The 4th Quarter Financial Statement

During our procedures relating to the budget, we noted the budget amounts recorded on the 4th Quarter Financial Statement did not agree to the original budget approved by Department for Local Government (DLG). The difference noted was \$395,792 for receipts and \$201,300 for expenditures. The DLG approved budget must be properly posted on the 4th Quarter Financial Statement in order for the County to accurately determine the total budget available for expenditures from each fund. We recommend the original budget be properly posted to the 4th Quarter Financial Statement.

County Judge/Executive Lewis Warrix' Response: Will correct.

Report On Compliance With Requirements
Applicable To Each Major Program And On Internal Control
Over Compliance In Accordance With OMB Circular A-133
(Continued)

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARDS PROGRAM
AUDIT

REPORTABLE CONDITIONS

Reference Number 2003-5

The County Should Improve Subrecipient Monitoring Policies And Procedures

The county's role as a pass through entity requires certain policies and procedures to be in place to monitor subrecipients, and there are certain improvements that should be made to the county's subrecipient monitoring system. First, the county should review and monitor the Industrial Foundation's budget, including the affect of each draw down request on the budget. Any significant variations between budgeted amounts and actual amounts should be investigated. Second, the county should monitor the subrecipient more closely for compliance with federal requirements (such as Davis-Bacon Act wage requirements, reporting requirements, etc.). Finally, the county should review and monitor periodic reports from the Industrial Foundation concerning relevant financial information as well as annual audits required to be performed in accordance with OMB Circular A-133. We recommend that the County institute these internal control improvements to the subrecipient monitoring system.

County Judge/Executive Lewis Warrix' Response: County will take a more active role in making sure Foundation reports are monitored.

Reference Number 2003-6

The County Should Maintain Adequate Records Regarding Federal Awards

The County's record keeping system related to federal awards should be improved. In addition to the records currently maintained, the county should maintain copies of draw down requests (including all supporting documentation, such as contractor invoices) and a breakdown of individual federal award amounts applied to each draw down request. We recommend that the county improve their record retention system as outlined.

County Judge/Executive Lewis Warrix' Response: Steps have been made to correct this situation.

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SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

BREATHITT COUNTY
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For The Fiscal Year Ended June 30, 2003

Federal Grantor Program Title <u>Grant Name (CFDA #)</u>	<u>Pass-Through Grantor's Number</u>	<u>Expenditures</u>
Cash Programs:		
<u>U.S. Department of Housing and Urban Development</u>		
Passed-Through State Department for Local Government:		
Community Development Block Grant (CFDA #14.228)	00-044	\$ 242,100
<u>U.S. Appalachian Regional Commission</u>		
Passed-Through State Department for Local Government:		
Appalachian Regional Commission Grants (CFDA #23.002)	Not Available	211,717
<u>U.S. Department of Agriculture</u>		
Passed-Through State:		
Rural Development Community Facilities Grant (CFDA #10.766)	Not Available	300,000
<u>U. S. Federal Emergency Management Agency</u>		
Passed-Through State Department of Military Affairs:		
Disaster and Emergency Assistance Grant (CFDA #83.544)	Not Available	17,027
<u>U.S. Department of Commerce</u>		
Passed Through National Oceanic Atmospheric Administration:		
Pride Community Grants- (CFDA #11.469)	Not Available	<u>77,524</u>
Total Expenditures of Federal Awards		<u>\$ 848,368</u>

BREATHITT COUNTY
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For The Fiscal Year Ended June 30, 2003

Note 1 - Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Breathitt County, Kentucky, and is presented on a modified cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

Note 2 - The federal expenditures include grants to subrecipients as follows:

<u>Subrecipient</u>	<u>Number</u>	<u>Pass-Through Grant Amount</u>
Breathitt County Industrial Foundation	00-044	\$242,100
Breathitt County Industrial Foundation	Not Available	\$211,717
Breathitt County Industrial Foundation	Not Available	\$300,000

CERTIFICATION OF COMPLIANCE -
LOCAL GOVERNMENT ECONOMIC ASSISTANCE AND DEVELOPMENT PROGRAMS

BREATHITT COUNTY FISCAL COURT

For The Fiscal Year Ended
June 30, 2003

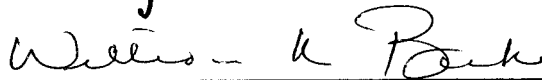
CERTIFICATION OF COMPLIANCE
LOCAL GOVERNMENT ECONOMIC ASSISTANCE AND DEVELOPMENT PROGRAMS
BREATHITT COUNTY FISCAL COURT

For The Fiscal Year Ended June 30, 2003

The Breathitt County Fiscal Court hereby certifies that assistance received from the Local Government Economic Development Program and Local Government Economic Assistance Program was expended for the purpose intended as dictated by the applicable Kentucky Revised Statutes.

A large, stylized handwritten signature in black ink, likely belonging to Lewis Warrick, is written over a horizontal line.

Lewis Warrick
County Judge/Executive

A handwritten signature in black ink, likely belonging to William K. Back, is written over a horizontal line.

William K. Back
County Treasurer

